The Future of the Open Trading System:

The Role of Japan

Address by Mr. Arthur Dunkel, Director-General, General Agreement on Tariffs and Trade, to the 12th Keidanren Forum, Tokyo, 1 July 1981

Trade relations are passing through a difficult phase: some would say their most difficult in more than 40 years.

It would have been very surprising, indeed almost miraculous, if these relations had not been affected by the unsatisfactory state of the world economy during the 70's.

Opinions differ, however, as to how far the open and fair trading system, based on the rules and cooperation established under the GATT, is really in danger. Is it still essentially intact? Or are its disciplines and guarantees being eroded? Doubts are also being expressed about the capacity of the system to contribute effectively to solving the problems which have emerged in international trade, and which have found expression in increasing protectionist pressures.

Against this background of strain and questioning, it is a challenge to be asked to talk about the "future of the open trading system". The challenge is even greater when I must speak in Japan, whose economy has drawn best advantage from the present trading system.

In such circumstances, the starting-point for a discussion of the future of this system must be an assessment of its state of health. In judging its performance, there is no need to look back very far. The contribution of the GATT system to the extraordinary post-war expansion of the world economy up to 1970 is generally acknowledged, and needs no defence by me.
The record of the 70's, however, deserves closer examination. It contains a mixture of positive, as well as less satisfactory, features.

Let us begin with the more comforting side of the picture.

The first point to underline is that, in spite of the breakdown of the Bretton Woods monetary system, in spite of the so-called "oil shocks", in spite of the effects of the recession in a number of specific industrial sectors, in spite of the need to introduce far-reaching regulation of trade in textiles, there has been no general resort to protectionism.

On the contrary, the successful conclusion of the Tokyo Round of multilateral trade negotiations has led to increased liberalization on a broad front, as well as to a revision and clarification of some of the most important trade rules. In other words, the GATT trading system has been significantly reinforced during the 70's. I am glad to be able to report that the commitments undertaken during these negotiations are being implemented faithfully. This means that the benefits of the Tokyo Round will spread through the 80's. Needless to say, this process is one of GATT's chief concerns for the new decade.

We can also be fairly satisfied about the present functioning of another main aspect of GATT's work, the settlement of particular trade disputes brought to it for conciliation.

One can therefore affirm that although governments remain subject to great pressures to introduce restrictive measures, and although they have yielded some ground in particular sectors, protectionism has on the whole been resisted.

It is worth asking why this should be so. Why have the worst economic difficulties since the 1930's not led to an outbreak of the kind of economic nationalism that marked the years of the Great Depression?

There are in fact a number of reasons, not least among them the existence of the GATT rules themselves. Essentially, governments know how greatly the prosperity of their countries depends on the existence of a liberal system of trade. They have tried, in consequence, to support one another, through GATT, in opposing protectionism. For all the major trading nations, economic interdependence has now reached such a point, and export and import interests are so inextricably woven together, that their governments rightly hesitate to take any trade measure that might provoke a chain reaction.

There is another element, new and welcome, in the present situation. The traditional trading nations could be expected to recognize that their economic health is linked with maintenance of open trade. Encouragingly, however, they are now increasingly being joined by the developing countries,
who are beginning to perceive the great advantages that the multilateral trading system offers to them.

Nevertheless, and this is the other side of the coin, there have recently been worrying signs that the current situation is deteriorating. Formal trade barriers have not, on the whole, been re-erected. But there has been, in particular, increasing resort to various forms of incentives to exports, and a proliferation of bilateral agreements to restrain trade. Bilateral disputes have arisen in unusual numbers, many concerning transatlantic trade, or trade with Japan. The recession is indeed leaving its mark on trade, as on other aspects of economic activity. With the volume of international trade growing, in total, by barely 1 per cent in 1980, against 6 per cent in 1979, and with the 1981 performance unlikely to be much better, competition in world markets was bound to be intense, and to generate frictions and conflicts.

Can we, however, assume that these new and more sophisticated forms of interference in trade flows will disappear when economic conditions improve? I fear they will not, although they may well grow less sharp. The reason is that, to a great extent, they reflect more fundamental problems: problems which need to be looked at without delay.

As one of the most successful of all the trading nations, Japan, along with its trading partners, cannot ignore these problems. If left unresolved, they could seriously damage the liberal international trading system which is the necessary complement to national market economies based on the principle of free enterprise. There is, however, another reason also for Japan in particular to direct its attention to these matters: it is Japan's own dynamism that, in one case after another, has shown that these previously unrecognized problems exist. The problems and opportunities of trade in the 80's and 90's are, I believe, being revealed by the reactions of international trade relations to the economic challenge of Japan. These reactions explain, in my view, why governments, businessmen and the press in industrialized countries seem almost obsessed at present with Japan's trade performance.

This apparent obsession is the result of a combination of admiration and misgiving, not to say fear. Admiration is felt for the way in which the Japanese economy has continued to forge ahead, weathering the oil shock noticeably better than the other industrialized countries in spite of its dependence on imported energy. Misgivings, on the other hand, are displayed in a reluctance to take up the competitive challenge posed by Japanese exports.

In some ways, these attitudes are strongly reminiscent of an earlier obsession, widespread in Europe ten or so years ago, with what was known as "le défi américain" - "the American challenge". And just as fears,
reasonable or not, of the American challenge helped to shape public opinion and policy in the 1960's and 1970's, present attitudes to Japan are influencing trade policies today.

We in GATT cannot, therefore, be indifferent to these fears. Indeed, in all my contacts with government officials, with businessmen and bankers, and with the press, I find myself questioned about Japan's trade performance. We have tried to respond by contributing, ourselves, to the analysis of what has been happening. My reply to those questions has been to put two more of my own. I have asked: Is not the Japanese economy's only fault, in fact, to have been more flexible, and more rapid than most of its competitors in meeting the challenges of international competition and of new market opportunities and technological progress? And if so, would not other countries be wrong to respond to Japanese competition by trying to isolate themselves from these dynamic forces of change?

This line of argument leads, of course, to the conclusion that protective measures are an inappropriate response by other countries to Japanese competition, and that if they want to grow they should instead accept the challenge, which means accepting the need for adjustments to their own economies. I have suggested that the challenge is all the more necessary to accept because the manner in which Japan's productive capacity has evolved and diversified makes one suspect that your country may be leading the way into a new phase of the industrial revolution.

The fact is, I believe, that a basic reason - perhaps the basic reason - for the upsurge of protectionist pressures in the past five to ten years has been the reluctance of some sectors in the long-established industrial trading countries to accept as equal partners the newcomers on the world trading scene. This reluctance has been reinforced by the present unfavourable economic climate.

Japan is of course not strictly a newcomer. We have only to look back a few years, however, to recognize that its impact on world markets is both quantitatively and qualitatively different from what it was in, say, the early 1960's. It is Japan's present performance that constitutes the most formidable new element in world trade. But Japan is not alone in presenting new challenges to the adaptability of the older trading powers. There is a whole range of other countries which are either entering world markets as effective competitors for the first time, or are already established but are now breaking into new sectors of the market.

To accept the newcomers to world trade is not easy, at the best of times - and these are not the best of times. It requires of the established trading countries or economic sectors that they be ready to change and adapt to the new competitive situation, and that they be ready, moreover, to continue adapting and changing as the situation continues to evolve. But change, however uncomfortable it may be, is a condition of economic growth.
To resist change is to deny the possibility of growth, to misallocate investment, to handicap those industries which can expect to benefit from change.

**Defending the multilateral system**

If this diagnosis is correct, and the present tensions in trade relations reflect, above all, the need to adjust to new competitive forces, what is the appropriate course for trade policy? What can be done? Japan, in particular, has already demonstrated its awareness of the social and political costs that adjustment can involve for its trading partners. But how should this awareness be translated into practice?

The worst possible course of action would be to leave problems to fester, or to allow positions to grow rigid. We in GATT have therefore been following with close attention the efforts of Japan to defuse some of the most visible difficulties in relations with your trading partners. We entirely support your aims. We can see that Japan and the other countries concerned are trying to avoid real deterioration in the climate of trade relations, an objective which is especially important at a time of strong protectionist pressures.

We cannot, however, help asking ourselves whether a search for short-term or ad hoc solutions, solutions that in some cases fall outside the multilateral trading system, may not be introducing some longer-term risks and rigidities, as well as setting undesirable precedents.

How can one economic sector be refused a solution that has been offered to another? How can one government deny to its businessmen what another country's government has conceded to their counterparts? Moreover, even if you cannot totally set aside the bilateral approach to the solution of particular trade problems, I see a great danger that the multilateral trading system as a whole will fall to pieces if this kind of solution becomes the rule. We all know the major examples of such bilateral solutions, of which the latest affect exports of automobiles; we all suspect that there are other such arrangements which have received no publicity. Each of these agreements has helped to deal with an immediate problem - but each has done so by going outside the established trading rules, and has thereby contributed to a cumulative erosion of the authority of those rules, and to obscuring the operation of the trading system as a whole.

Such a piecemeal approach aimed at solving particular problems, which are always presented as being exceptions to the rule, must also surely strengthen the dangerous bilateral approach to trade. It draws attention away from multilateral trade flows. It gives importance to those bilateral imbalances which ought to be without significance in a multilateral system, and puts a heavy and unfair responsibility on Japan itself.
It would be pointless to express such doubts about the approach now being followed if there were not an alternative course of action that might be capable of redressing present difficulties without the danger of storing up longer-term problems. That alternative is to place greater reliance on the opportunities available for resolving trade difficulties within the GATT system.

I assume we all agree that one of the great virtues of the present multilateral trading system is that governments acting under its rules not only are provided with objective criteria for their actions, but also are assured that these criteria are the same for all countries, large and small. If we accept, as your government and others have recently reaffirmed, that this framework of rules is essential, having proved its worth over more than a generation, can we then really believe that trade problems will find a lasting solution in actions divorced from those criteria and outside that framework? Is it possible for any government to continue for long to act in such a way in its relations with its trading partners and with the economic sectors concerned?

You will not be surprised if I, as Director-General of GATT, believe that the interests of all countries will be best served by relying, to the greatest possible extent, on the defences offered to them by the rule of the existing law of trade. And if it should appear that those defences are in some way inadequate, I would argue that the proper course is not to abandon them, but to reinforce them so that they can respond to present-day needs.

If today Japan and its trading partners feel that their mutual trading problems cannot be met by recourse to the established rules of GATT, then the conclusion I would draw is not that the rules should be side-stepped. We ought instead to be looking at the rules themselves. Do the GATT rules ensure adequate conditions for the process of adjustment? A GATT working group is in fact just starting to explore this field. What is the relevance of the continuing negotiations on the adequacy of the GATT rules on safeguards? These are the kind of questions we should be asking.

A similar reinforcement of the multilateral rules may be needed in the area of agricultural trade, which accounts for a strikingly large proportion of the total number of specific trade disputes at present subject to the GATT conciliation procedures. There are persistent, and in my view justified, complaints by agricultural exporting countries that their concerns have consistently received less attention than they should, and that the results of the Tokyo Round were much less substantial in the agricultural sector than for manufactures. Worldwide, the main trade restrictions are now undoubtedly in this sector. This is as true of Japan as it is of most other industrialized countries.
Adjustment, both in industry and in agriculture, is highly relevant to a third main field for action to strengthen the open trading system. This is the growing participation in international trade of the developing countries. As I mentioned earlier, these countries are beginning to perceive the advantages that the multilateral system offers to them. Progress in bringing them more fully into that system was made in the Tokyo Round. Much more undoubtedly remains to be done. In part, action will have to be multilateral in character, as it was when some GATT rules were adapted to their needs. But there is room for bilateral action by individual countries as well, and I shall have something to say on this later, in relation to what Japan might do.

The rôle of Japan

As you are perhaps aware, I have in recent months been led on several occasions to take a strong stand in favour of adjustment to the changing competitive situation. And this has required that I defend Japan's position in international trade relations. I have done so with a clear conscience. I trust that, having in a sense established my credentials, you in turn will be prepared to listen to some suggestions.

I should like first, and with some hesitation, to raise with you some possible Japanese responses to present difficulties, and then to conclude with a broader point concerning Japan's rôle in the multilateral trading system.

It is very hard, I find, to persuade people that the crucial issue in present trade difficulties involving Japan is not Japan itself, but the urgent need, revealed by your country's economic breakthrough, for these other countries to adapt. This effort of persuasion would be greatly facilitated if Japan, for its part, would find it appropriate to look at some aspects of its own import policy, as a contribution to carrying forward the dialogue with your trading partners, and to shifting the debate onto more constructive ground.

One such aspect is that Japan maintains relatively high import duties, as well as quantitative restrictions, on certain agricultural and tropical products, in both processed and unprocessed form. I know of a number of Japan's trading partners, developed and developing, whose export interest in these products is as great as that of Japan in other areas.

Your low average tariff, even after the harmonizing tariff cuts of the Tokyo Round, still conceals a number of peaks on specific products - peaks which protect processing activities carried out on imported raw materials. These activities could equally well take place in the countries of origin of the products concerned. Many are developing countries.
Going beyond the traditional instruments of trade policy, I need not tell you that Japan has, rightly or wrongly, the reputation among businessmen everywhere of being an exceedingly difficult market to penetrate. As Director-General of GATT, I know that Japan cannot fairly be accused of maintaining more trade restrictions than other industrialized countries. Most difficulties in exporting to Japan - communication, the wholesale and retail distribution system, established purchasing patterns - can only be tackled through energetic sales efforts. I am aware of the cooperation your authorities have offered to help in bringing about contacts between the Japanese business community and the foreign exporter, particularly with regard to achieving a more open distribution system. I hope there will be a strong response to this initiative. There is a further question of foreign investment in Japan, but this is a matter which I do not feel competent to examine. Finally, however, there remains the residue of complaints by exporters to Japan about what they see as specific, and in some cases deliberate, hindrances to their efforts. I believe it would be in Japan's interest to respond to these complaints, for instance by establishing some kind of investigative procedure to see if they were well-founded. This might well help to demonstrate Japan's commitment to open trading policies.

An advantage of your current surplus is of course that it has permitted an increase in the flow of investment from Japan to other countries, helped by the most welcome dismantling of restrictions on capital outflows. This should contribute to easing difficulties in trade relations. Employment-creating investment in countries where the impact of Japanese exports has been felt most strongly should help to moderate resistance to those exports. And such investments will also help to create relationships that may make it easier for exports from the countries concerned to enter the Japanese market. This latter aspect could be particularly important for relations between Japan and the developing countries.

These suggestions and thoughts are put forward with some diffidence. Their value can be judged only by someone with a much greater knowledge of Japanese trade than mine. I should however like to make a further point on which I believe I can speak with some confidence and authority.

Japan has whole-heartedly accepted the challenges of competition in world markets, and has displayed extraordinary energy, discipline and innovation in doing so. But a condition of your success has undoubtedly been the existence of an open multilateral trading system. No country has made better use of that system than Japan. No country would lose more if the effectiveness of the system were allowed to erode.

It was understandable that Japan did not, in earlier years, seek leadership in the multilateral trading system. You joined GATT only some years after it came into effect. Japan's share in world trade was then much smaller.
than it is now. The world economy was still in the middle of an extraordinary
twenty-five year boom that transformed living standards in most of the indus-
trialized world. But the situation has since changed greatly. Economic
growth has slowed down; new stresses have appeared in international trade
relations; the principles of multilateral cooperation and an open trading
system are being challenged. At the same time, Japan has emerged both as
one of the most dynamic and powerful trading nations and as the main focus of
pressures for bilateralism and protectionism.

In such circumstances, should not Japan be lending its full weight to
efforts to reinforce the multilateral trading system on which its economic
success has been built?

I am convinced it should.

Eight years ago, Japan provided the launching-pad for the Tokyo Round of
multilateral trade negotiations. Some of us saw the Tokyo meeting as a
most welcome sign that your country was now ready to take the initiative in
efforts to extend and strengthen the open trading system. I hope very much
that, in the years ahead, the promise which we detected in 1973 will be
fulfilled. Japan needs a strong and healthy multilateral trading system.
And that system, in turn, has need of whole-hearted and active Japanese
commitment and - dare I say it? - leadership.

The opportunities for such leadership are now presenting themselves, as
the GATT member countries, faced by a range of complex and potentially
disruptive issues, begin to draw the conclusion that they will need to enter
into a new phase in their cooperation if they are to meet successfully the
trade challenges of the 1980's. Only five days ago, GATT's Consultative
Group of Eighteen, a group of high trade policy officials, concluded - and I
quote - "that it would be useful to consider at the political level the
overall condition of the trading system". To this end, there was broad
agreement that - and I quote again - "it would be appropriate for the GATT
Contracting Parties to envisage convening a ministerial meeting during 1982.
Adequate preparation for such a meeting would be essential, and for this
purpose an analysis would need to be carried out of the issues confronting
the trading system and of the trends and problems likely to emerge in the
1980's".

Clearly, these conclusions point out a new direction for the work of
GATT, and by implication for the trade relations between the GATT member
countries. An opportunity is opening up both for surmounting present
difficulties, and for continuing to expand the benefits which the world
draws from the open trading system. It is an opportunity which I believe
ought to be seized.

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